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No. 95-928

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

JOHN W. ATHERTON, JR.,
Petitioner,
v.
FEDERAL DEPOSIT INSURANCE CORPORATION,
AS RECEIVER FOR CITY SAVINGS, F.S.B.,
Respondent.

On Writ of Certiorari to the
United States Court of Appeals
for the Third Circuit

BRIEF FOR PETITIONER

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QUESTIONS PRESENTED

1. Whether, in suits for money damages brought by the Resolution Trust Corporation (RTC) against directors or officers of failed federally chartered depository institutions, the gross negligence standard of 12 U.S.C. § 1821(k) (1994), enacted as part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (FIRREA), supplants any federal common law simple negligence standard that may have pre-dated FIRREA.

2. Whether, even if § 1821(k) does not supplant federal common law, federal courts are nevertheless precluded from applying any federal common law standard of liability to the conduct of directors and officers of federally chartered depository institutions in light of *O'Melveny & Myers v. FDIC*, 114 S. Ct. 2048 (1994).

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The opinion of the court of appeals (Pet. App. A2-A50) is reported at 57 F.3d 1231. The decision of the United States District Court for the District of New Jersey (Pet. App. A57-A67) is not reported.

JURISDICTION

The court of appeals issued its decision on June 23, 1995 (Pet. App. A2-A50). A timely petition for rehearing with request for rehearing *en banc* was denied on September 14, 1995 (Pet. App. A55-A56). The judgment of the court of appeals was issued on September 22, 1995 (Pet. App. A51-A53). The petition for a writ of certiorari was filed on December 12, 1995, and was granted on April 15, 1996. 116 S. Ct. 1415 (1996). The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

12 U.S.C. § 1821(k) (1994):

Liability of directors and officers. A director or officer of an insured depository institution may be held personally liable for monetary damages in any civil action by, on behalf of, or at the request or direction of the Corporation, which action is prosecuted wholly or partially for the benefit of the Corporation—

(1) acting as conservator or receiver of such institution,

(2) acting based upon a suit, claim, or cause of action purchased from, assigned by, or otherwise conveyed by such receiver or conservator, or

(3) acting based upon a suit, claim, or cause of action purchased from, assigned by, or otherwise conveyed in whole or in part by an insured depository institution or its affiliate in connection with assistance provided under section 1823 of this title,

for gross negligence, including any similar conduct or conduct that demonstrates a greater disregard of a duty of care (than

gross negligence) including intentional tortious conduct, as such terms are defined and determined under applicable State law. Nothing in this paragraph shall impair or affect any right of the Corporation under other applicable law.

STATEMENT OF THE CASE

In 1989, Congress enacted § 212(k) of the Financial Institutions, Reform, Recovery, and Enforcement Act of 1989 (FIRREA), codified at 12 U.S.C. § 1821(k) (§ 1821(k) or Section 1821(k)), which provides that a director or officer of an insured depository institution may be held personally liable for money damages in a suit brought by the RTC[1] as receiver of such institution "for gross negligence" or "conduct that demonstrates a greater disregard of a duty of care (than gross negligence)." A "savings clause" of § 1821(k) provides that nothing in § 1821(k) shall impair or affect any right of the RTC under "other applicable law."

This case presents for review a divided decision by a three-judge panel of the Third Circuit in which the majority held that (i) § 1821(k) has no applicability to federally chartered depository institutions; (ii) because of the savings clause, § 1821(k) does not displace allegedly pre-existing federal common law claims against directors and officers of federally chartered institutions; (iii) state law has no applicability to federally chartered institutions; and (iv) therefore, the RTC may only assert federal common law claims against the directors and officers of federally chartered institutions.

The majority's position, rejected by four other federal circuits, should be reversed because it is in clear conflict with decisions of this Court, most particularly, the Court's recent decision in *O'Melveny & Myers v. FDIC*, 114 S. Ct. 2048 (1994).

[1] Pursuant to 12 U.S.C. § 1441a(m)(1) (1994), the RTC ceased to exist on December 31, 1995, and was succeeded in all its capacities by the Federal Deposit Insurance Corporation (FDIC) on that date. Accordingly, the FDIC has been substituted for the RTC as the respondent in this case.

1. The Applicable Statutory Framework

Before and after the enactment of FIRREA in 1989, both the states and the federal government granted charters permitting institutions to conduct business as savings associations and savings banks, *i.e.*, institutions whose charters traditionally required or encouraged longer term deposits than conventional banks and greater investment in home mortgages and related loans.[2] Before FIRREA, state chartered savings associations were authorized, but not required, to obtain federal insurance of their deposit accounts from the Federal Savings and Loan Insurance Corporation (FSLIC) pursuant to Title IV of the National Housing Act, 12 U.S.C. §§ 1724-1730i (repealed 1989). The FSLIC was a federal agency under the direction of the Federal Home Loan Bank Board (FHLBB), 12 U.S.C. § 1725(a) (repealed 1989), which promulgated regulations on behalf of the FSLIC. State chartered savings associations that obtained FSLIC insurance of deposits became subject to a degree of federal regulation.

In contrast to state chartered savings associations, federally chartered savings associations before FIRREA were chartered and regulated by the FHLBB under the Home Owners' Loan Act of 1933 (HOLA). 12 U.S.C. §§ 1461-1470 (1988). These institutions were required to have federal deposit insurance, generally through the FSLIC. 12 U.S.C. § 1726(a) (repealed 1989).[3] By virtue of their federal charters, federal savings associations were subject to greater regulation by the FHLBB of their lending, investment, deposit-taking, branching and general business operations than were state chartered institutions. *See, e.g.*, 12 C.F.R. §§ 545.1-.142 (1989). These savings associations

[2] In the interest of brevity, the term "savings association" used throughout the rest of this brief will include both savings associations and savings banks.

[3] An exception not relevant here allowed certain institutions that had converted from state to federal charters to retain the FDIC insurance they held when they operated under state charters. *See* 12 U.S.C. § 1464(o) (1988); § 1726(a) (repealed 1989).

were also subject to the regulations governing all FSLIC-insured institutions.

In the event of receivership of any FSLIC-insured depository institution before FIRREA, the FSLIC was required to be appointed receiver of a federal savings association, 12 U.S.C. § 1464(d) (1988), and under most circumstances generally could be appointed receiver of a state chartered savings association as well, 12 U.S.C. § 1729(c) (repealed 1989).

FIRREA abolished both the FSLIC and the FHLBB. FIRREA § 401(a), 103 Stat. at 354. After FIRREA, the deposits of all federally insured savings associations, whether chartered under state or federal law, became insured by the FDIC. 12 U.S.C. §§ 1814, 1815. FIRREA created the Office of Thrift Supervision (OTS) within the Department of the Treasury, 12 U.S.C. § 1462a, and gave the Director of OTS authority to charter and regulate federal savings associations. 12 U.S.C. §§ 1463(a), 1464(a). The OTS also was granted direct statutory responsibility to regulate certain aspects of the operations of all savings associations, whether chartered under state or federal law, including in particular, their compliance with required capital and liquidity levels. 12 U.S.C. §§ 1464(t), 1465.

In the event of receivership, FIRREA required the RTC to be appointed receiver of any savings association, whether chartered under state or federal law, until the termination of the RTC on December 31, 1995. Since that time, the FDIC has been required to be appointed such receiver. *See* 12 U.S.C. §§ 1441a(b)(3), 1464(d)(2)(E)(ii). FIRREA also enacted provisions expanding upon the authority of the RTC and FDIC as receiver beyond the authority previously contained in the applicable statutes relating to the FDIC, including through the enactment of § 1821(k). 12 U.S.C. § 1821.

2. The Proceedings Below

Petitioner, John W. Atherton, Jr., was a former director and officer of City Federal Savings Bank (City Federal), a federally chartered, federally insured savings bank that was headquartered in Bedminster, New Jersey. City Federal was declared insolvent by the OTS in December 1989, at which time the RTC was appointed as receiver of City Federal. (First Am. Compl. ¶¶ 5, 6, 14.)

The RTC, in its capacity as receiver of City Federal and for City Federal's successors in receivership and conservatorship, brought this civil action for money damages against petitioner and other former directors and/or officers of City Federal in 1993. The RTC alleged that petitioner and the other former City Federal directors and officers were liable for breaching their duty of care in connection with losses incurred by City Federal on three real estate acquisition, development and construction loans City Federal made in the mid-1980s. The loans went into default in the late 1980s during the nationwide collapse of the commercial real estate market. The RTC did not assert that any of the defendants engaged in any fraud, self dealing, conflict of interest, unjust enrichment or other breach of their duty of loyalty. Rather, the RTC claimed only that the defendants failed to discharge properly their duty of care as directors and officers of City Federal in connection with their consideration, approval and oversight of the three subject loans. (*Id.* ¶¶ 70-72.)

The RTC's original complaint, filed in April 1993, and its first amended complaint, filed two months later, alleged in a single count claims for negligence, gross negligence and breach of fiduciary duty under both state and federal common law. (*Id.* ¶¶ 71-72.) Neither pleading asserted any claim against the defendants predicated on the statutory standard of liability contained in § 1821(k).

Petitioner and other defendants below moved to dismiss the RTC's first amended complaint on grounds that § 1821(k) established gross negligence as the exclusive standard of liability in suits against former directors and officers of failed federally chartered depository institutions. The RTC chose to concede that state law was not applicable because City Federal was a federally chartered institution. However, the RTC argued that

the last sentence of § 1821(k), the so-called "savings clause," preserved the right for the RTC to proceed against the defendants under "federal common law," which the RTC asserted establishes an "ordinary" or "simple" negligence standard of liability.

On November 15, 1993, the district court granted the defendants' motions and dismissed the RTC's first amended complaint to the extent it alleged claims based other than upon § 1821(k). (Pet. App. A58-A64.) The district court held that § 1821(k) established a uniform federal gross negligence standard of liability in cases involving federally chartered institutions and displaced any claims under federal common law. (*Id.* at A62-A64.) The district court also held that the RTC had withdrawn its state law claims. (*Id.* at A64.)

The RTC then filed a second amended complaint that asserted claims against the defendants based solely on § 1821(k). The RTC also moved to certify the district court's ruling on the standard of liability issue for immediate appeal to the United States Court of Appeals for the Third Circuit pursuant to 28 U.S.C. § 1292(b). The district court granted the RTC's motion (*id.* at A65), and, on May 18, 1994, the court of appeals granted the RTC's request for permission to appeal (*id.* at A68). In its appeal, the RTC did not challenge or seek review of the district court's ruling that the RTC had withdrawn its state law claims.

On June 23, 1995, a divided panel of the court of appeals reversed the district court. 57 F.3d 1231, Pet. App. A1-A50. The majority opinion states:

> We hold that Congress [in enacting Section 1821(k)] did not . . . supplant federal common law holding directors and officers liable for conduct less culpable than gross negligence. . . . [W]e will reverse the district court's order and direct the court to permit the RTC to pursue any claims for negligence or breach of fiduciary duty available as a matter of federal common law.

57 F.3d at 1249, Pet. App. A37 (footnote omitted). The majority opinion, 57 F.3d at 1244, Pet. App. A27-A28, purports to follow the Court's instruction in *City of Milwaukee v. Illinois*, 451 U.S. 304 (1981), that the dispositive question regarding whether Congress has displaced a federal common law claim is "whether the legislative scheme 'spoke directly to a question' [previously addressed by federal common law]," *id.* at 315 (paraphrasing *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1978)). The majority, however, immediately proceeds to disregard entirely the first sentence of § 1821(k), establishing a gross negligence standard, and concludes that Congress evidenced a clear intent to preserve any pre-existing federal common law claim for simple negligence based solely upon the majority's reading, in isolation, of the last sentence of § 1821(k), the "savings clause." *Id.* at 1237-38, 1245, Pet. App. A27-30, A37.

The savings clause states that "[n]othing in this paragraph shall impair or affect any right of the Corporation under other applicable law." 12 U.S.C. § 1821(k). It follows, however, the first sentence of § 1821(k), which states in pertinent part that "[a] director or officer of an insured depository institution may be held personally liable . . . in any civil action by . . . the Corporation . . . for gross negligence, including . . . conduct that demonstrates a greater disregard of a duty of care (than gross negligence) . . . ." *Id.* The Third Circuit majority reads the savings clause, without regard to the preceding sentence of § 1821(k), as preserving for the RTC the right to assert claims against directors and officers of federally chartered depository institutions under federal common law. 57 F.3d at 1245, Pet. App. A37.

The majority purports to find support for its interpretation of the savings clause in the legislative history of FIRREA. *Id.* at 1238-42, 1245, Pet. App. A28-33, A37. The majority concludes that, in adopting § 1821(k), Congress intended to do no more than preempt so-called "insulating" statutes that had been enacted by various states in recent years and that established a higher standard of care than gross negligence, *e.g.*, intentional

misconduct, for directors and officers of depository institutions chartered in those states. *Id.* at 1242, Pet. App. A31.

To avoid the inevitable conclusion that in the first sentence of § 1821(k) Congress "spoke directly" to the standard of liability issue regarding officers and directors of federally chartered institutions, the majority, based on its aforementioned reading of the statute's legislative history, concludes "that Congress did not intend § 1821(k) to apply to federally-chartered depository institutions" and that "the RTC *cannot* proceed under § 1821(k) in the City Federal action." *Id.* at 1249 n.17, Pet. App. A37 (emphasis in original).

The majority assumes that there existed prior to FIRREA a federal common law claim against directors and officers of federally chartered institutions derived from *Briggs v. Spaulding*, 141 U.S. 132 (1891), and its progeny, but leaves it to the district court to decide whether such claim is for simple negligence or gross negligence. 57 F.3d at 1247, n.16, Pet. App. A32.

In a forceful opinion concurring in part[4] and dissenting in relevant part, Circuit Judge Mansmann argues that the majority's conclusion conflicts with the plain language of § 1821(k). 57

[4] In the court of appeals, this case was consolidated with *RTC v. Schuster*, a case involving claims by the RTC as receiver of United Savings and Loan of Trenton, New Jersey (United Savings), against former directors and officers of United Savings. 57 F.3d at 1234-35, Pet. App. A7-A9. United Savings was a state chartered depository institution, and the RTC sued the defendants in *Schuster* for negligence and breach of fiduciary duty under New Jersey law. *Id.* The defendants in *Schuster* filed a motion for dismissal and summary judgment as to the RTC's claims on grounds that § 1821(k) preempted the RTC's state law claims. *Id.* The district court in *Schuster* denied the motion, holding that § 1821(k) did not preempt the state law claims, and the Third Circuit panel, including Judge Mansmann, unanimously affirmed the district court. *Id.* To petitioner's knowledge, the defendants in *Schuster* did not file a petition for a writ of certiorari regarding the circuit court's ruling in that case. In this case, whether the savings clause preempts state law claims is not an issue. As noted above, in the district court below, the RTC chose to withdraw the state law claims it had

(footnote continues)

F.3d at 1249-55, Pet. App. A38-A44 (Mansmann, J., concurring in part and dissenting in relevant part). Judge Mansmann observes that § 1821(k), by its clear terms, applies to every "insured depository institution," a term defined in 12 U.S.C. § 1813(c)(2) to include all depository institutions, whether federally or state chartered, the deposits of which are insured by the FDIC. 57 F.3d at 1251, Pet. App. A40.

Citing this Court's decision in *City of Milwaukee*, 451 U.S. 304, Judge Mansmann concludes that Congress "spoke directly" to the issue of the standard of liability for directors and officers of federally chartered depository institutions when Congress enacted § 1821(k). *Id.* at 1252, Pet. App. A44. As a result, Judge Mansmann states that she would have held, as the Fifth, Sixth, Seventh and Tenth Circuits have previously held, that federal common law "must yield" to § 1821(k) in cases such as this. *Id.* at 1249, Pet. App. A38.

Following the decision by the court of appeals, petitioner and other defendants below sought rehearing, with a suggestion of a rehearing *en banc*. The court of appeals denied the petition for rehearing on September 14, 1995. Pet. App. A55-A56. Since the filing of the petition for a writ of certiorari on December 12, 1995, five of the six original petitioners have settled with the RTC, or the FDIC as the RTC's successor, and have withdrawn as petitioners, leaving John W. Atherton, Jr., as the sole remaining petitioner.

(footnote continued)

asserted against the petitioner and the other defendants in this case. The district court ruled that the RTC had withdrawn its state law claims (Pet. App. A64), and the RTC did not appeal from that ruling.

SUMMARY OF ARGUMENT

I. Because federal common law is always "subject to the paramount authority of Congress," *New Jersey v. New York*, 283 U.S. 336, 348 (1938), the determinative question regarding whether a congressional statute displaces a pre-existing federal common law rule is "whether [Congress] 'spoke directly to [the] question' " previously governed by such rule. *City of Milwaukee v. Illinois*, 451 U.S. 304, 315 (1981) (paraphrasing *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1978)). In § 1821(k), Congress "spoke directly" to the applicable standard of liability in suits by the RTC against the directors and officers of failed federally chartered savings associations. Thus, § 1821(k) provides that directors and officers of "insured depository institution[s]" — a statutory term defined to include both federally chartered and state chartered savings associations such as City Federal — shall be liable for "gross negligence, including . . . conduct that demonstrates a greater disregard of duty of care (than gross negligence) . . . ." There is no legitimate basis for federal judges to decide that directors and officers of federally chartered depository institutions should be liable under a purported pre-existing federal common law simple negligence standard when Congress has provided in § 1821(k) that they may be liable for gross negligence or *greater* disregard of a duty of care.

Four federal courts of appeals have decided that § 1821(k) supplants any pre-existing federal common law simple negligence standard. *RTC v. Frates*, 52 F.3d 295, 297 (10th Cir. 1995); *FDIC v. Bates*, 42 F.3d 369, 373 (6th Cir. 1994); *RTC v. Miramon*, 22 F.3d 1357, 1364 (5th Cir. 1994); *RTC v. Gallagher*, 10 F.3d 416, 424 (7th Cir. 1993). Only the Third Circuit majority concludes otherwise based upon its reading of the savings clause of § 1821(k). The majority interprets the phrase "other applicable law" in the savings clause to embrace "*all*" applicable law, including any pre-existing federal common law claims for simple negligence. 57 F.3d at 1237-38, 1245, Pet. App. A28-31, A37

(emphasis in original). The majority's position is fatally defective for two overriding reasons.

First, in the process of violating elementary rules of statutory construction, the majority renders the substantive provision of § 1821(k), articulating the gross negligence standard, a nullity insofar as federally chartered institutions are concerned. It defies reason that Congress, in the first sentence of § 1821(k), would authorize a statutory cause of action for gross negligence *or greater* against federally chartered institutions "and in the next sentence to eviscerate that standard by allowing actions under federal common law for simple negligence." *Gallagher*, 10 F.3d at 420. In an apparent attempt to avoid the incongruity of this result, the majority adopts the wholly untenable position that § 1821(k) simply does not apply to federally chartered institutions. That conclusion, however, was too much even for the respondent to accept. It concedes that § 1821(k) clearly applies to federally chartered institutions. *See* Br. for the Resp. in Opp. at 12.

Second, in addition to misreading the plain wording and meaning of § 1821(k), the Third Circuit majority also mischaracterizes the legislative history of that provision. According to the majority, § 1821(k) had but a single purpose, to wit, to preempt state "insulating" statutes that exonerated directors and officers from liability even for conduct that was grossly negligent. 57 F.3d at 1242, Pet. App. A30. The legislative history clearly establishes, however, that Congress had more than one concern in enacting § 1821(k). Overcoming the effect of state insulating statutes was one such concern. Respect for federalism principles was another concern, which caused Congress not to seek to preempt state laws that allowed directors and officers to be sued for simple negligence. But undeniably a third concern of Congress that informed § 1821(k) was Congress's understanding that imposing too strict a federal liability standard on directors and officers would discourage qualified individuals from serving

as such in the financial institution industry. Accordingly, in drafting § 1821(k), Congress sought to address each of these concerns: by permitting the RTC to sue for simple negligence in those states that allowed such suits, by allowing it to sue for gross negligence in those states that had adopted "insulating" statutes, and by allowing it to sue for gross negligence in the case of any federally chartered savings association.

II. In any event, there is no federal common law standard of liability that the federal courts may properly apply to the conduct of directors and officers of federally chartered savings associations because none of the extraordinary circumstances that justify the application of federal common law are present here. Such circumstances exist only when there is " 'a significant conflict between some federal policy or interest and the use of state law.' " *O'Melveny & Myers v. FDIC*, 114 S. Ct. 2048, 2055 (1994) (quoting *Wallis v. Pan Am. Petrol. Corp.*, 384 U.S. 63, 68 (1966)). No such "significant conflict" is present here. Thus, no "rights of the United States arising under nationwide federal programs," *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 726 (1979), are at issue. *O'Melveny*, 114 S. Ct. at 2055. Nor has Congress anywhere authorized federal courts to apply any federal common law standards of liability to the directors and officers of federally chartered depository institutions. Moreover, because the governing statute for federal savings associations not in receivership, HOLA, is comprehensive, but does not even tangentially touch on the subject of director or officer liability, there is no basis for the interstitial use of federal common law in this case. As the Court made clear in *O'Melveny*: "Nor would we adopt a court-made rule to supplement federal statutory regulation that is comprehensive and detailed; matters left unaddressed in such a scheme are presumably left subject to the disposition provided by state law." 114 S. Ct. at 2054.

The fact that City Federal was federally chartered does not justify the application of any uniform federal common law standard in determining the liability of its directors and officers. A federal charter does not create a need for uniformity regarding

an issue that falls squarely within two traditional areas of state law (torts and corporation law). This is particularly so here, where, in the context of a comprehensive legislative scheme, Congress in § 1821(k) voiced its preference for the use of "applicable State law" to define "gross negligence." Congress thereby clearly evidenced its view that there does not exist any overriding federal policy in favor of a uniform federal standard of liability, except to the extent expressly provided for in § 1821(k). *See Reconstruction Fin. Corp. v. Beaver County*, 328 U.S. 204, 209 (1946) (where part of regulatory scheme relies on state law, "assumption" that uniformity is necessary cannot be made).

Nothing in the Court's earlier decisions in *Briggs v. Spaulding*, 141 U.S. 132 (1891), or *Bowerman v. Hamner*, 250 U.S. 504 (1919), requires a different conclusion. Those decisions, which respondent claims established a federal common law simple negligence standard for the directors and officers of depository institutions, were decided long before *Erie R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938), which declared that "[t]here is no federal general common law," a principle reaffirmed in *O'Melveny*, 114 S. Ct. at 2053. Moreover, there has been no consensus in the federal courts that *Briggs* or *Bowerman* establish a simple negligence standard. Indeed, the respondent in this very case admits that "[t]he content of the federal common law standard . . . is not clearly established." Br. for the Resp. in Opp. at 16-17. Accordingly, it cannot plausibly be argued that federal common law should be applied to the directors and officers of federally chartered institutions to assure that the liability standards for all such directors and officers will be uniform. It never has been.

Despite several lower court cases holding the contrary, the internal affairs doctrine, which provides that the law of the state of incorporation normally determines issues relating to the internal affairs of a corporation, has no application here. Not only is the doctrine a conflict of laws principle that properly applies only where a choice must be made between the laws of two or more states, *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982), application

of the doctrine to the liability of directors and officers of federally chartered associations is inconsistent with *O'Melveny*, as a number of recent federal court cases have recognized.

For the foregoing reasons, as explained in further detail hereafter, petitioner respectfully submits that the only claims that the RTC or FDIC should be able to assert against the directors and officers of failed federally chartered savings associations are (1) claims for gross negligence under § 1821(k), or (2) claims for simple negligence under state law if the applicable state recognizes such claims.[5]

ARGUMENT

I. THE GROSS NEGLIGENCE STANDARD OF § 1821(k) DISPLACES ANY PRE-EXISTING FEDERAL COMMON LAW SIMPLE NEGLIGENCE STANDARD

As shown in Part II of this brief, no federal common law negligence claim lay against the petitioner even before, much less after, the adoption of FIRREA. The Court does not have to make that determination, however, because, in any event, the gross negligence standard of § 1821(k) displaces any pre-existing federal common law simple negligence standard. The courts of appeals for the Fifth, Sixth, Seventh and Tenth circuits, correctly applying long-established precedents of this Court, have so ruled in unanimous opinions. *RTC v. Frates*, 52 F.3d 295, 297 (10th Cir. 1995); *FDIC v. Bates*, 42 F.3d 369, 373 (6th Cir. 1994); *RTC v. Miramon*, 22 F.3d 1357, 1364 (5th Cir. 1994); *RTC v. Gallagher*, 10 F.3d 416, 424 (7th Cir. 1993). At the circuit court level, only the divided Third Circuit decision under review herein has reached a contrary conclusion.

[5] In this case, of course, the RTC's state law claims have been withdrawn, so it may proceed only under § 1821(k).

A. When Congress "Speaks Directly" To An Issue Previously Governed By Federal Common Law, That Common Law Is Displaced

This Court has "always recognized that federal common law is 'subject to the paramount authority of Congress.' " *City of Milwaukee v. Illinois*, 451 U.S. 304, 313 (1981) (quoting *New Jersey v. New York*, 283 U.S. 336, 348 (1931)). Because of federalism concerns, "the appropriate analysis in determining if federal statutory law governs a question previously the subject of federal common law is not the same as that employed in deciding if federal law pre-empts state law." *Id.* at 316. When considering state law preemption, this Court assumes "that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." *Id.* (internal quotation marks omitted). By contrast, when the question is whether congressional legislation displaces federal common law, "[s]uch concerns are not implicated in the same fashion . . . , and accordingly the same sort of evidence of a clear and manifest purpose is not required." *Id.* at 316-17. The Court assumes "that it is for Congress, not federal courts, to articulate the appropriate standards to be applied as a matter of federal law." *Id.* at 317.

Congress has enacted an extensive series of statutory provisions applicable to federally chartered savings associations and to the RTC (and FDIC) as receiver of such savings associations. *See, e.g.*, 12 U.S.C. §§ 1461-1468c, 1811-1834b. Under this statutory scheme, first the FHLBB, and since the adoption of FIRREA, the OTS, were granted "plenary authority" by Congress to regulate the operations of federally chartered savings associations. 12 U.S.C. § 1464(a); *Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 144 (1982). This "comprehensive program" of statutory provisions by itself "strongly suggests that there is no room for courts to attempt to improve on that program with federal common law." *City of Milwaukee*, 451 U.S. at 319.

The Third Circuit majority "reject[s]" the argument that any federal common law standard of director and officer liability

"was supplanted because of the scope of FIRREA." 57 F.3d at 1247, Pet. App. A33. The majority argues that in *City of Milwaukee*, express language in the subject act's legislative history demonstrated the establishment of a "comprehensive program," but that no such language exists in FIRREA itself or in its legislative history. *Id.* The majority overlooks its own description of FIRREA as "a massive 371-page legislative package," *id.* at 1239, the legislative history of FIRREA stating that the statute's delineation of RTC rights as receiver is "comprehensive," H.R. Rep. No. 54, 101st Cong., 1st Sess., pt. I, at 415 (1989), and this Court's description of FIRREA as "comprehensive legislation," *O'Melveny & Myers v. FDIC*, 114 S. Ct. 2048, 2054 (1994).

More fundamentally, Congress does not have to "address every issue" of an area previously governed by federal common law, *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1978), nor must it have "affirmatively proscribed the use of federal common law," to abrogate its application. *City of Milwaukee*, 451 U.S. at 315; *accord United States v. Texas*, 507 U.S. 529, 534 (1993); *Astoria Fed. Sav. & Loan Ass'n v. Solimino*, 501 U.S. 104, 108-109 (1991) (there is no requirement of "clear statement" or "strict construction"). Rather, whenever Congress "speak[s] directly" to the matter previously addressed by federal common law, such federal common law is displaced. *Texas*, 507 U.S. at 534; *City of Milwaukee*, 451 U.S. at 315; *Northwest Airlines, Inc. v. Transport Workers Union*, 451 U.S. 77, 95 n.34 (1981); *Mobil Oil*, 436 U.S. at 625. Congress did just that in § 1821(k).[6]

[6] The "speak directly" test is satisfied by the "natural meaning" of a statutory provision, *Isbrandtsen Co. v. Johnson*, 343 U.S. 779, 783 (1952), by a statutory listing of powers that omits the power claimed to exist under the common law, *id.* at 789, by a statutory provision that would be rendered "superfluous" by continued application of a common law rule, *Astoria*, 501 U.S. at 112, or by an "implication" after application of the traditional tools of statutory interpretation, *id.* at 110. Each of these is present here. *See infra* pp. 17-21.

B. In § 1821(k), Congress "Spoke Directly" To The Issue Of The Standard Of Liability Applicable To Directors And Officers Of Federally Chartered Depository Institutions

In determining whether Congress "spoke directly" to the standard of liability that governs suits brought by the RTC against officers and directors of failed federally chartered depository institutions in § 1821(k), the guiding principle is that "[t]he starting point for the interpretation of a statute 'is the language of the statute itself. Absent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive.' " *Kaiser Aluminum & Chem. Corp. v. Bonjorno*, 494 U.S. 827, 835 (1990) (quoting *Consumer Product Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980)).

Section 1821(k) is in two parts: a substantive provision contained in the first sentence of § 1821(k) and a so-called "savings clause" set forth in the second sentence. In its first sentence, § 1821(k) provides in pertinent part that

> [a] director or officer of an insured depository institution may be held personally liable for monetary damages in any civil action by . . . the Corporation[7] . . . acting as conservator or receiver of such institution, . . . for gross negligence, including any similar conduct or conduct that demonstrates a greater disregard of a

[7] The term "Corporation" as used in § 1821(k) refers to the FDIC. 12 U.S.C. § 1811(a) (1994). While § 1821(k) by its terms applies only to actions brought by the FDIC as conservator or receiver of failed insured depository institutions, the RTC is vested with "the same powers and rights to carry out its duties with respect to institutions [for which it is appointed conservator or receiver] as the [FDIC] has under" § 1821(k) and other sections of the Federal Deposit Insurance Act. 12 U.S.C. § 1441a(b)(4)(A) (1994).

duty of care (than gross negligence) including intentional tortious conduct, as such terms are defined and determined under applicable State law.

The savings clause provides that "[n]othing in this paragraph shall impair or affect any right of the Corporation under other applicable law."

The first sentence of § 1821(k) "speak[s] directly," and with unmistakable clarity, to the standard of liability that governs civil actions such as this one, *i.e.*, money damage suits by the RTC against the directors and officers of failed federally insured depository institutions.[8] It provides that directors and officers "may be held personally liable . . . for gross negligence, including . . . conduct that demonstrates a *greater* disregard of a duty of care (than gross negligence) . . . ." (emphasis added). While not explicitly stating that directors and officers may *not* also be found liable for simple negligence, that conclusion flows inexorably from the plain wording of the first sentence of § 1821(k); otherwise there would have been no reason for Congress to specify that directors and officers may be liable for gross negligence "*including* . . . conduct that demonstrates a *greater* disregard of a duty of care (than gross negligence)." *Id.* (emphasis added).

In its brief opposing the petition for certiorari, the FDIC argues that if the first sentence of § 1821(k) were intended to restrict the RTC from suing for simple negligence, "it would most naturally have provided that the [RTC] 'may (and may only)' sue for gross (or greater) negligence." Br. for the Resp. in Opp. at 9. But the use of the additional words "and may only" would have been entirely superfluous. By providing that directors and officers may be liable for "gross negligence, including . . . conduct that demonstrates a *greater* disregard of a duty of

[8] As will be discussed, *infra* pp. 22-25, and contrary to the holding of the majority below, it is indisputable that the first sentence of § 1821(k) applies to both federal and state chartered "insured depository institution[s]," and the FDIC has so conceded, *see* Br. for the Resp. in Opp. at 12.

care" (emphasis added), it was unnecessary to add that they may not be liable for conduct demonstrating a *lesser* disregard of a duty of care.

Because the substantive provision of § 1821(k) "speak[s] directly" to the question previously addressed by a purported body of federal common law, namely, the appropriate liability standard to be applied in suits brought by the RTC against directors and officers of failed federally insured depository institutions, any such preexisting federal common law standard is displaced. *Texas*, 507 U.S. at 534; *Astoria*, 501 U.S. at 108; *City of Milwaukee*, 451 U.S. at 315; *Northwest Airlines*, 451 U.S. at 95 n.34; *Mobil Oil*, 436 U.S. at 625. There is no legitimate basis for federal judges to decide that directors and officers should be liable, under federal common law, for simple negligence when Congress has provided, as a matter of federal statutory law, that they should be liable for gross negligence or greater. As the Fifth Circuit accurately observed in *RTC v. Miramon*, "It is difficult to conceive how Congress could more clearly 'speak directly' to the issue of the standard of care for personal liability of directors and officers of federally-insured depository institutions." 22 F.3d 1357, 1361 (5th Cir. 1994). *See also RTC v. Gallagher*, 10 F.3d 416, 420 (7th Cir. 1993) ("It is hard to imagine a more definitive statement by Congress that a gross negligence standard of liability applies to cases brought by the RTC against officers and directors of failed financial institutions.").

The majority opinion correctly identifies " 'the language of the statute itself' " as the appropriate " 'starting point' " for interpreting whether § 1821(k) displaces any preexisting federal common law claim for simple negligence. 57 F.3d at 1237, Pet. App. A13 (quoting *Kaiser Aluminum*, 494 U.S. at 835). Rather than proceeding to read § 1821(k) in its entirety, however, the majority opinion instead completely disregards the first, substantive provision of the statute, and asserts that "[t]he disposition of these appeals turns on the breadth of § 1821(k)'s last sentence," the so-called "savings clause." *Id.* As noted above, that clause provides that "[n]othing in this paragraph shall impair or affect

any right of the Corporation under other applicable law." 12 U.S.C. § 1821(k). According to the majority, the savings clause, read in isolation, manifests Congress's intent to preserve the RTC's ability to seek recovery from directors and officers under all "other applicable law" including federal common law.[9]

[9] The majority opinion predicates its reading of the savings clause on two arguments: (1) elsewhere in FIRREA, when Congress wanted to limit its reference to the laws of a particular jurisdiction, it did so with specific language; and (2) the majority's reading of the savings clause is consistent with this Court's decision in *Patterson v. Shumate*, 504 U.S. 753, 759 (1992), where the phrase "applicable nonbankruptcy law" was interpreted to encompass "any relevant nonbankruptcy law, including federal law such as ERISA." 57 F.3d at 1238, Pet. App. A14. The Court in *Patterson*, however, noted that "the plain language of the [statute] is our determinant," 504 U.S. at 757, and found in that case that no other language in the subject statute suggested that the phrase "applicable nonbankruptcy law" referred only to state laws, *id.* at 758. In the absence of any such other language, the Court in *Patterson* found corroborative support for a broad reading of the phrase at issue in the fact that elsewhere in that statute Congress had expressly referenced state law when it sought to so limit the scope of applicable laws. *Id.* at 758-59. *Patterson* might be an apt precedent for the majority's reliance on other provisions in FIRREA expressly referencing state law if the savings clause of § 1821(k) is read in total isolation, as the majority in fact reads it. But the savings clause does not constitute all of § 1821(k); rather, it follows the first sentence of that section, and its scope must be informed by the plain meaning of the language used in that first sentence, *see United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 242 n.5 (1989) (courts should not read bankruptcy statute "in an unnatural way . . . that is inconsistent with the remainder" of the statute). Because the first sentence of § 1821(k) "speak[s] directly" to the issue of the standard of liability applicable to directors and officers of federally chartered depository institutions, any pre-existing federal common law standard is displaced. *See City of Milwaukee*, 451 U.S. at 315-16. Thus, unlike the statute in *Patterson*, § 1821(k) does contain specific language that "suggests that the phrase ['other applicable laws'] refers . . . exclusively to *state* law." 504 U.S. at 758 (emphasis in original). Under these circumstances, the fact that elsewhere in FIRREA Congress refers expressly to state laws is not sufficient to override Congress's clear displacement of federal common law by virtue of having "spoke[n] directly" to the issue of director and officer liability in § 1821(k) itself. Long-established rules of statutory construction

(footnote continues)

57 F.3d at 1237, Pet. App. A13. In so ruling, however, the majority effectively renders the first sentence of § 1821(k) a nullity, at least insofar as federally chartered institutions (which allegedly are subject to federal common law) are concerned.

If the majority's reading of the savings clause is adopted, it perforce leads to the conclusion that by enacting § 1821(k), Congress gave the RTC a choice: the RTC could sue a director or officer of a failed federally chartered depository institution for gross negligence under the first sentence of § 1821(k) or, alternatively, by virtue of the savings clause, the RTC could sue for simple negligence under federal common law. But offering the RTC this election would be nonsensical. As the Fifth Circuit so cogently remarked in *Miramon*, "Why would the RTC ever bring an action under section 1821(k), where it would have to prove gross negligence, when it could bring an action under the federal common law and only be required to prove simple negligence?" 22 F.3d at 1361. *See also Gallagher*, 10 F.3d at 420 ("It is illogical that Congress intended in one sentence to establish a gross negligence standard of liability and in the next sentence to eviscerate that standard by allowing actions under federal common law for simple negligence."); *FDIC v. Bates*, 42 F.3d 369, 372 (6th Cir. 1994) ("If the court reads the savings clause to preserve simple negligence claims, then the gross negligence standard explicitly articulated in the savings clause is redundant, meaningless surplusage."). It is, of course, an " 'elementary canon of construction that a statute should be interpreted so as not to render one part inoperative.' " *Mountain States Tel. & Tel. Co. v. Pueblo of Santa Ana*, 472 U.S. 237, 249 (1985) (quoting *Colautti v. Franklin*, 439 U.S. 379, 392 (1979)). *See also Astoria*, 501 U.S. at

(footnote continued)

require courts to read statutes in a manner that affords internal consistency, *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 370 (1986), avoids rendering superfluous any parts thereof, *Astoria*, 501 U.S. at 112; *United States v. Menasche*, 348 U.S. 528, 538-39 (1955), and recognizes that specific language controls general language, *D. Ginsberg & Sons v. Popkin*, 285 U.S. 204, 208 (1932).

112 ("[W]e construe statutes, where possible, so as to avoid rendering superfluous any parts thereof.").

C. Section 1821(k) Clearly Applies To Federally Chartered Depository Institutions Such As City Federal

If it had been Congress's intent that the directors and officers of federally chartered depository institutions should be liable for simple negligence under pre-existing federal common law — and, therefore, its intent that federal common law be embraced within the phrase "other applicable law" in the savings clause — then Congress could have achieved that result in at least two different ways: (1) merely by excluding federally chartered institutions from the coverage of § 1821(k) or (2) by drafting a savings clause that expressly preserved "federal common law" claims, as it has done in other comprehensive federal statutory schemes.[10] The Third Circuit majority, apparently cognizant of at least the first alternative, and in an attempt both to side-step the "speak directly" test and to achieve logical consistency between the first sentence of § 1821(k) and the majority's expansive interpretation of the savings clause, baldly declares that § 1821(k) does not apply to federally chartered depository institutions. The majority thus states, "Congress did not intend to address the liability standards applicable to directors and officers of federally chartered institutions in enacting § 1821(k),

[10] *See, e.g.*, Comprehensive Environmental Response, Compensation, and Liability Act of 1980, 42 U.S.C. § 9608(d)(2) (1994) ("Nothing in this subsection shall be construed to limit any other State or Federal statutory, contractual, or common law liability of a guarantor . . . ."); Emergency Planning and Community Right-to-Know Act of 1986, 42 U.S.C. § 11046(g) (1994) ("Nothing in this section shall restrict or expand any right which any person (or class of persons) may have under any Federal or State statute or common law to seek enforcement of any requirement or to seek any other relief . . . ."); Hazardous and Solid Waste Amendments of 1984, 42 U.S.C. § 6991b(d)(3) (1994) ("Nothing in this subsection shall be construed to limit any other State or Federal statutory, contractual or common law liability of a guarantor . . . ."); Resource Conservation and Recovery Act of 1976, 42 U.S.C. § 6924(t)(3) (1994) (same).

but rather enacted the provision for the purpose of preempting state insulating statutes." 57 F.3d at 1246, Pet. App. A31.

According to the majority, § 1821(k) was "a reaction to the enactment by various states, during the middle and late 1980s, of lenient director liability statutes that protected directors from gross negligence claims by limiting their liability to instances of reckless, willful and wanton boardroom misconduct." *Id.* at 1239, Pet. App. A16. Thus, according to the majority, Congress's sole purpose in enacting § 1821(k) was to permit the RTC, when suing the directors or officers of a state chartered institution, to proceed under the gross negligence standard of § 1821(k) in those states that had enacted insulating statutes and, as permitted by the savings clause, to proceed under simple negligence standards in those states that had not enacted insulating statutes and otherwise followed simple negligence standards. *Id.* at 1242, Pet. App. A34 ("[T]he legislative history [of Section 1821(k)] reflects an effort to ensure that directors and officers of state-chartered institutions . . . not escape liability to the RTC under the shield of certain state laws that had effectively insulated them even from claims based on their grossly negligent or reckless conduct.").

The majority's position suffers from two fatal defects: (1) it ignores and is at odds with the plain meaning of the terms used in § 1821(k) as defined elsewhere in FIRREA; and (2) it erroneously concludes that Congress had only one purpose in mind (preempting state insulating statutes) in adopting § 1821(k).

The first fatal flaw in the Third Circuit majority's position, as Judge Mansmann's dissent correctly recognizes, 57 F.3d at 1251, Pet. App. A41-A42, is that § 1821(k), by its own terms, quite evidently is intended to apply to RTC suits against directors and officers of federally chartered institutions as well as those of state chartered institutions. Thus, § 1821(k) provides that the RTC may bring an action against a director or officer of an "insured depository institution." The term "insured depository institution" is defined in FIRREA as "any bank or savings association the deposits of which are insured by the [FDIC]."

12 U.S.C. § 1813(c)(2). The term "savings association" is defined in FIRREA to include "any Federal savings association" and "any State savings association." 12 U.S.C. § 1813(b)(1)(A), (B). The term "Federal savings association" is defined to include "any Federal savings association or Federal savings bank which is chartered under [12 U.S.C. § 1464]." 12 U.S.C. § 1813(b)(2).[11] Moreover, the statutory definitions in FIRREA contain separate definitions for "Federal depository institution" and "State depository institution." 12 U.S.C. § 1813(c)(4), (5). The former term is defined to include "any Federal savings association" which, as indicated, is defined as any federally chartered savings association or savings bank. 12 U.S.C. § 1813(c)(4). If, as the Third Circuit majority ruled, Congress intended the gross negligence standard of § 1821(k) to apply only to directors or officers of state chartered institutions, it would have referred in § 1821(k) to insured "State depository institution[s]," not to "insured depository institution[s]," a term that embraces federal as well as state depository institutions. Significantly, in opposing the certiorari petition herein, the FDIC candidly acknowledged the Third Circuit majority's fundamental error. It stated, "We agree with petitioners that [Section 1821(k)] should be read to apply to federally chartered institutions." Br. for the Resp. in Opp. at 12.

Since there is no question but that § 1821(k) applies to federally chartered as well as state chartered institutions, the task of statutory interpretation is to reconcile the first sentence of § 1821(k) with the savings clause so that both are given coherent meanings that are applicable to both types of institutions. *See*

[11] City Federal, whose full name at the time of its receivership in December 1989 was City Federal Savings Bank, was insured by the FDIC and was a federal savings bank chartered under 12 U.S.C. § 1464. (First Am. Compl. ¶ 5.) Therefore, City Federal was clearly a "Federal savings bank" referred to in 12 U.S.C. § 1813(b)(2), a "Federal savings association" as defined in 12 U.S.C. § 1813(b)(2), a "savings association" as defined in 12 U.S.C. § 1813(b)(1)(A), and an "insured depository institution" as defined in 12 U.S.C. § 1813(c)(2) and as used in § 1821(k). Accordingly, § 1821(k) clearly applies to the RTC's suit against petitioner, a former director and officer of City Federal.

Ron Pair, 489 U.S. at 242 n.5. We submit this is achieved by ruling that, in the case of a federally chartered institution, the RTC may sue directors and officers for gross negligence, as the first sentence of § 1821(k) provides, and that the RTC may not alternatively sue them for simple negligence under federal common law because (1) the first sentence of § 1821(k) implicitly precludes a suit for simple negligence under § 1821(k) itself, and (2) the savings clause cannot be read to permit a federal common law simple negligence claim without nullifying the application of the first sentence of § 1821(k) to federally chartered institutions. In the case of a state chartered institution, the first sentence of § 1821(k) can be read to permit the RTC to sue its directors and officers for gross negligence even in those states that have enacted insulating statutes and the savings clause can be read to allow the RTC to sue for simple negligence in those states that have adopted a simple negligence standard.[12]

D. The Legislative History Of § 1821(k) Demonstrates That Congress Intended To Establish A Gross Negligence Federal Standard Of Liability

As noted above, the majority's reading of the legislative history of § 1821(k) also suffers from a fatal defect, *i.e.*, the failure to recognize that the language of the statute reflects a congressional effort to harmonize several competing concerns; it does not reflect a single legislative purpose. A fair reading of all

[12] The above interpretation assumes *arguendo* that a federal common law claim for simple negligence against directors and officers of a federally chartered depository institution existed before FIRREA. As demonstrated in Part II, that is not the case. Rather, the cause of action available to such an institution against its directors and officers prior to the institution's placement into conservatorship or receivership is under state law. Accordingly, the correct reading of the first sentence of § 1821(k) is that in the case of both a federally chartered and a state chartered savings association, the RTC may sue its directors and officers for gross negligence even though the applicable state law would otherwise require a higher standard, and the savings clause should be read as allowing the RTC to sue for simple negligence in those relatively few states that have adopted a simple negligence standard.

the legislative history of § 1821(k) supports the construction of that statute adopted by the Fifth, Sixth, Seventh and Tenth Circuits as well as by Judge Mansmann in her dissent below.

In enacting § 1821(k), Congress had at least three concerns. First, as the majority correctly observes, Congress attributed at least part of the savings and loan debacle of the 1980s to director and officer malfeasance and concluded that state insulating statutes, in those states that had enacted them, stood as an obstacle to recovery even from directors and officers who had been grossly negligent in the performance of their duties. 57 F.3d at 1238-39, Pet. App. A15-A16. Accordingly, one of the purposes of establishing a gross negligence standard in § 1821(k), as explained by the Senate bill's floor manager, Senator Riegle, was to preempt state laws that established a higher duty of care. 135 Cong. Rec. S4278-79 (daily ed. Apr. 19, 1989); *see also RTC v. Miramon,* 22 F.3d 1357, 1363 n.9 (5th Cir. 1994).

In its recitation of the legislative history of § 1821(k), however, the Third Circuit majority simply disregards the fact that there was a second substantial concern that informed the drafting of that provision. While there clearly was a recognition in Congress that state insulating statutes may have gone too far in exonerating grossly negligent directors and officers of failed depository institutions, there undeniably was also a recognition, among legislators and others, that if liability standards were made too stringent, qualified persons would be dissuaded from serving. As one student of the history of § 1821(k) has observed:

> [D]espite the reports of scandalous excesses by individual bank and thrift directors, a number of legislators and financial experts worried that an excessively zealous federal crackdown against directors of depository institutions might ultimately harm the public interest by scaring away from the banks and thrifts some of their most qualified and honest managers — just the sort of leaders who were now most needed to revive and salvage those institutions.

David B. Fischer, *Bank Director Liability Under FIRREA: A New Defense for Directors and Officers of Insolvent Depository Institutions — Or a Tighter Noose?,* 39 UCLA L. Rev. 1703, 1709 (1992) (footnote omitted).[13]

This concern explains, at least in part, why the standard of liability in § 1821(k) was set at gross negligence rather than simple negligence. The Senate's initial bill, reported from the Senate Banking Committee to the full Senate on April 13, 1989, would have allowed the RTC to bring claims not only for "gross negligence" and "willful misconduct" but also for "any cause of action available at common law" including ordinary "negligence." S. 774, 101st Cong., 1st Sess. § 214(n) (1989). Within the week, however, Senators Riegle and Garn introduced a managers' amendment to the bill that eliminated all reference to "any cause of action available at common law" and "negligence." Under the amended language, directors and officers could only be found liable in suits by the RTC for "gross negligence or intentional tortious conduct." 135 Cong. Rec. S4452.

In the course of the floor debate on the managers' amendment, Senator Sanford, a member of the Senate Banking Committee from which the bill originated, made clear that, at least in his mind, the change in the bill from a simple negligence to a gross negligence standard was critical from the perspective of attracting qualified individuals to serve as directors and officers of depository institutions. He stated:

> Mr. President, I would like to thank the distinguished managers of the bill, Senator Riegle and Senator Garn, for including in the managers' amendment modifications to the bill regarding directors and officers liability

[13] *See also Prosecuting Fraud in the Thrift Industry: Hearings on H.R. 1278 Before the Subcomm. On Criminal Justice of the House Comm. On the Judiciary,* 101st Cong., 1st Sess. 98-99 (1989) (testimony of John K. Villa, banking attorney and author); *id.* at 278-79 (testimony of Edward L. Yingling, executive director of government relations, American Bankers' Association).

insurance contracts, surety bond, and financial institution bond contracts, *and provisions relating to State laws affecting the liability of officers and directors of financial institutions.*

I believe that these changes are essential if we are to attract qualified officers and directors to serve in our financial institutions.

Id. at S4276.

Courts of appeals that have held § 1821(k) displaces federal common law have also read the legislative history of that provision as manifesting a congressional intent, in part, to adopt a liability standard that would not discourage qualified individuals from serving as directors and officers of financial institutions. For example, the Seventh Circuit stated in *RTC v. Gallagher:*

> Congress was aware that the proposed simple negligence standard might make it difficult for financial institutions to attract high quality officers and directors. . . .
>
> . . . Senator Sanford's contemporaneous understanding of the managers' amendment as establishing a federal gross negligence standard of liability necessary to enable financial institutions to attract quality officers and directors supports our interpretation of the plain language of § 1821(k).

10 F.3d 416, 422-23 (7th Cir. 1993). *See also FDIC v. Bates*, 42 F.3d 369, 373 (6th Cir. 1994) ("[C]omments during the debate reflected concern that authorizing a claim under simple negligence would keep qualified people from seeking or retaining positions as officers and directors.").[14]

[14] The change in the standard of care from simple to gross negligence reflected in part the third concern of Congress regarding § 1821(k), *i.e.*, that Congress not preempt all state laws establishing duties of care for

(footnote continues)

The Third Circuit majority disputes that § 1821(k) "manifest[s] Congressional intent to adopt a uniform gross negligence standard of care for directors and officers of bankrupt federally insured depository institutions." 57 F.3d at 1242, Pet. App. A23. But it is clear from the Senate floor debate that at least some Senators, including one of the floor managers of the Senate bill, perceived § 1821(k) as establishing a uniform federal standard of care and that such standard was gross negligence. Thus, Senator Garn, one of the bill's managers, stated on April 19, 1989, after the language of the bill had been changed to eliminate reference to ordinary negligence, "*[W]e impose* on directors and officers of [a] federally insured financial institution *a standard of care* they owe to the institution and its shareholders." 135 Cong. Rec. S4281 (daily ed. Apr. 19, 1989) (emphasis added). Senator Roth similarly observed that the amended bill "*sets a standard of care* owed to the financial institution because it is federally insured." *Id.* (emphasis added). Senator Roth added, "I think it is important to point out that *the standard of care imposed* is owed to the institution and its shareholders. . . . [W]e are talking about the *standard of care owed* to an institution that enjoys Federal Deposit Insurance." *Id.* (emphasis added).

The House version of § 1821(k), H.R. 1278, 101st Cong., 1st Sess. § 212(k) (1989), which passed after the Senate version and is the version that eventually became law, preserved the Senate's removal of the simple negligence standard. *See* Pub. L. No. 101-73, § 212(k), 103 Stat. 183, 243 (1989). The House-Senate Conference Report, which represents the final statement of terms agreed upon by both houses of Congress, confirms that

(footnote continued)

directors and officers. Thus, in introducing the managers' amendment, Senator Riegle explained:

> The reported bill totally preempted State law in this area with respect to suits brought by the FDIC against bank directors or officers. However, in light of the State law implications raised by this provision, the managers' amendment scales back the scope of this preemption.

135 Cong. Rec. S4278-4279.

Congress decided upon a gross negligence standard for § 1821(k):

> Title II preempts State law with respect to claims brought by the FDIC in any capacity against officers or directors of an insured depository institution. The preemption allows the FDIC to pursue claims for gross negligence or any conduct that demonstrates a greater disregard of a duty of care, including intentional tortious conduct.

H.R. Conf. Rep. No. 222, 101st Cong. 1st Sess. 398 (1989), *reprinted in* 1989 U.S.C.C.A.N. 432, 437.

The Third Circuit majority gives far more weight to the report of the Senate Banking Committee (Banking Committee Report), published in the *Congressional Record* on June 19, 1989, than to the House-Senate Conference Report. According to the majority, the Banking Committee Report "makes clear that § 1821(k) did not disturb any claims, available as a matter of state or federal law, that would hold directors and officers liable for conduct less culpable than gross negligence." 57 F.3d at 1241, Pet. App. A20. The Banking Committee Report stated:

> This subsection does not prevent the FDIC from pursuing claims under State law or under other applicable Federal law, if such law permits the officers or directors of a financial institution to be sued (1) for violating a lower standard of care, such as simple negligence, or (2) on an alternative theory such as breach of contract or breach of fiduciary duty.

S. Rep. No. 19, 101st Cong., 1st Sess. 318 (double star print 1989).

The Banking Committee Report is of only limited utility in interpreting congressional intent. *See, e.g., RTC v. Miramon,* 22 F.3d 1357, 1362 (5th Cir. 1994) ("[E]xamination of all of the legislative history, and scrutiny of the sequence of events leading up to the bill's passage, calls into question the conclusion of [the Banking Committee] report."). In the first place, it is not clear

that the authors of the Banking Committee Report, when referring to "other applicable Federal law," had in mind federal common law. They nowhere specifically so state.[15] But even if that is what they intended, their intent was not made clear to the Senate when it voted on and passed the amended bill, S. 774, 101st Cong., 1st Sess. § 214(n) (1989). That vote took place on April 19, 1989, but the Banking Committee Report was not published until two months later, 135 Cong. Rec. S6907, S6934 (daily ed. June 19, 1989). In *Clarke v. Securities Industry Ass'n,* 479 U.S. 388, 407 (1987), the Court refused to "attach substantial weight" to a statement placed in the Congressional Record by a sponsor of an act ten days after the law was passed.

It is true, as the Third Circuit majority points out, that the Banking Committee Report was available some six weeks before § 1821(k) was finally enacted into law in early August 1989. 57 F.3d at 1241, Pet. App. A20. But it is not at all clear, given the timing of its issuance, that the Report accurately reflected the views of the members of the Senate, much less those of House members, when final votes were cast. The House-Senate Conference Report does not suffer from these infirmities and is entitled to greater weight. It nowhere suggests that the RTC may pursue a claim for simple negligence but, on the contrary, indicates that it may "pursue claims for gross negligence or any conduct that demonstrates a greater disregard of a duty of care, including intentional tortious conduct." H.R. Conf. Rep. No. 222 at 398.

Although the legislative history of § 1821(k) is limited and not entirely free from ambiguity, it strongly suggests that Congress intended to limit the liability of directors and officers of depository institutions to gross negligence except, in deference

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[15] It is just as likely that "other applicable Federal law" referred to the administrative enforcement provisions of FIRREA, *see, e.g.,* 12 U.S.C. § 1818, and/or to other federal statutes that might be used as a basis for suits against bank officers and directors, *e.g.*, the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (1994). That is what the court concluded in *Gallagher,* 10 F.3d at 420: "A better reading of the savings clause is that it was drafted to preserve the RTC's ability to take other regulatory actions based on simple negligence."

to principles of federalism, in those cases where a lesser standard of care is imposed under the law of a particular state. Nothing in the legislative history demonstrates that Congress, in enacting the final version of § 1821(k), intended that the directors and officers of federally chartered institutions should be subject to a simple negligence standard under federal common law.

The Court's analysis should begin where *City of Milwaukee*, *Northwest Airlines* and *Mobil Oil* begin, and with what the majority below ignored, the substantive language of § 1821(k). Because § 1821(k) "speak[s] directly" to the standard of liability applicable to directors and officers of federally chartered institutions, and because it imposes a gross negligence standard, it should be deemed to supplant any federal common law simple negligence standard that may have existed before FIRREA. The Court's analysis need proceed no further.

II. IN ANY EVENT, THERE IS NO FEDERAL COMMON LAW CLAIM FOR ORDINARY NEGLIGENCE APPLICABLE TO OFFICERS AND DIRECTORS OF FEDERALLY CHARTERED DEPOSITORY INSTITUTIONS

If this Court should determine that § 1821(k) does not create a gross negligence standard of liability that supplants any pre-existing federal common law simple negligence standard, then, alternatively, we ask the Court to rule that no such federal common law standard existed prior to the adoption of FIRREA, nor does any such standard now exist; rather, the liability of directors and officers of federally chartered depository institutions should be determined as a matter of state law, not federal common law.

A. There Is No Established Federal Common Law Standard Of Liability

Respondent contends that "the federal common law standard of liability for officers and directors of federally chartered depository institutions is ordinary negligence" and relies for that proposition on two decisions of this Court, *Briggs v. Spaulding*,

141 U.S. 132 (1891), and *Bowerman v. Hamner*, 250 U.S. 504 (1919). Br. for the Resp. in Opp. at 17. The Third Circuit majority similarly notes that "the Supreme Court first articulated a common law standard of care for directors and officers of federally chartered depository institutions over 100 years ago in *Briggs* . . . ." 57 F.3d at 1247 n.16, Pet. App. A32.[16]

We dispute that *Briggs* and *Bowerman* intended to create an ordinary negligence liability standard for officers and directors (regardless of whether viewed as a federal or state common law standard). Rather, we believe those cases hold bank directors and officers liable only for gross negligence. In *Briggs*, the Supreme Court considered whether two directors of a federally chartered bank could be held liable for losses caused by unlawful loans made by its officers that the directors failed to discover. In dismissing claims by the bank's receiver, the Court stated, in a passage relied upon by the RTC as establishing a federal common law simple negligence standard of liability, that the "degree of care" required of bank directors "is that which ordinarily prudent and diligent men would exercise under similar circumstances . . . ." *Briggs*, 141 U.S. at 152. But in a subsequent, critical passage, the Court elaborated as follows:

> [W]e hold that directors must exercise ordinary care and prudence in the administration of the affairs of a bank, and that this includes something more than officiating as figure-heads. They are entitled under the law to commit the banking business, as defined, to their duly-authorized officers, but this does not absolve them from the duty of reasonable supervision, nor ought they to be permitted to be shielded from liability because of want of knowledge of wrong-doing, if that ignorance is the result of *gross inattention* . . . .

[16] The majority stated, however, that "[g]iven our conclusion that § 1821(k) does not address the liability of directors and officers of federally chartered institutions, we need not discern whether the federal common law standard is one of ordinary or gross negligence." *Id.*

Id. at 165-66 (emphasis added).

In short, "it is evident that the Court [in *Briggs*] was not applying the heightened standard of care simple negligence envisions." *Washington Bancorp. v. Said,* 812 F. Supp. 1256, 1266 (D.D.C. 1993). Similarly, in *Bowerman*, a bank director was held personally liable for bank losses because he never attended a single director's meeting during the bank's entire 5½ year existence, did not exercise even "slight care" in the discharge of his responsibilities, and "deliberately avoided acquiring knowledge of [the bank's] affairs and wholly abdicated the duty of supervision and control which rested upon him as a director." 250 U.S. at 509, 510-11. The Court concluded that "in this case we have the *gross negligence* of the appellant." *Id.* at 511. *See generally* Fischer, 39 UCLA L. Rev. at 1712-26.

B. *O'Melveny* Confirms That There Is No Federal General Common Law

Even if *Briggs* and *Bowerman* did in fact create a simple negligence standard of liability, they no longer settle the issue of whether there is a federal common law ordinary negligence standard upon which the RTC may predicate a claim against the petitioner because those cases were decided well before the Court's decision in *Erie,* which declared that "[t]here is no federal general common law." 304 U.S. at 78.

The *Erie* admonition was recently reaffirmed by a unanimous Court in *O'Melveny & Myers v. FDIC,* 114 S. Ct. 2048 (1994). There, the FDIC as receiver of a failed state chartered, federally insured savings and loan association brought state law causes of action for professional negligence and breach of fiduciary duty against a law firm that had represented the institution. *Id.* at 2052. The law firm moved for summary judgment on grounds that, *inter alia,* under state law, the knowledge of the conduct of the institution's officers must be imputed to the institution and to the FDIC as its receiver, and that, because of the imputed knowledge, the FDIC was estopped from pursuing its claims against the law firm. *Id.* The FDIC countered that a

federal common law rule, not state law, determined the imputation question. *Id.* The Court disagreed. *Id.* at 2052-56. It determined that there was no explicit federal statutory provision that displaced applicable state law, *id.* at 2054; that given the comprehensiveness of FIRREA, there was no justification for creating federal common law exceptions to supplement it, *id.*; and that, apart from FIRREA, the use of state law would not produce a conflict with any identifiable federal policy or interest, *id.* at 2055-56. Accordingly, the Court concluded that "this is not one of those extraordinary cases in which the judicial creation of a federal rule of decision is warranted." *Id.* at 2056.

No decision of this Court subsequent to *Erie* has recognized the existence of a federal common law claim for negligence against the directors or officers of any insured depository institution.[17] There have been lower federal court decisions post-*Erie* that have relied on *Briggs* and *Bowerman* to recognize a federal common law claim for breach of the duty of care against directors and officers of federally chartered depository institutions. *See, e.g., FDIC v. Bierman,* 2 F.3d 1424, 1432 (7th Cir. 1993); *FDIC v Appling,* 992 F.2d 1109, 1113-14 (10th Cir. 1993); *Hoehn v. Crews,* 144 F.2d 665, 672 (10th Cir. 1944), *aff'd on other grounds sub nom. Garber v. Crews,* 324 U.S. 200 (1945); *Michelsen v. Penney,* 135 F.2d 409, 419 (2d Cir. 1943); *FDIC v. Mason,* 115 F.2d 548, 551 (3d. Cir 1940); *Atherton v. Anderson,* 99 F.2d 883, 887 (6th Cir. 1938). These cases, however, merely assume that the application of federal common law is appropriate. None engages in the type of analysis that the Court's more recent decisions — particularly *O'Melveny* — have deemed essential before deciding to apply a federal common law rule in lieu of a state law rule.[18]

[17] The Court has cited *Briggs* only once since *Erie,* in a footnote in a dissenting opinion in *Bangor Punta Opers. Inc. v. Bangor & Aroostook R. Co.,* 417 U.S. 703, 721 n.1 (1974) (Marshall, J., dissenting). Since *Erie*, the Court has never cited *Bowerman.*

[18] The Third Circuit majority acknowledged that *Briggs* was decided prior to *Erie*, but citing *Bierman* and *Appling* concluded that "the *Briggs* articulation of the standard of care apparently continues to apply as a matter of federal common law." 57 F.3d at 1247, n.16, Pet. App. A32.

Although, as *O'Melveny* indicates, the creation of federal common law is reserved for "extraordinary cases," 114 S. Ct. at 2056, the Court has recognized the need and authority of federal courts to create federal common law in a "few and restricted" instances, *Wheeldin v. Wheeler*, 373 U.S. 647, 651 (1963). Such instances exist only when there is "a significant conflict between some federal policy or interest and the use of state law." *Wallis v. Pan Am. Petrol. Corp.*, 384 U.S. 63, 68 (1966). As the Court said in *O'Melveny*, "Our cases uniformly require the existence of such a conflict as a precondition for recognition of a federal rule of decision." 114 S. Ct. at 2055. In this way, the court grants proper deference to Congress's paramount authority to promulgate laws and to the requirements of federalism and the Rules of Decision Act, 28 U.S.C. § 1652, that state law be applied unless there is a clear and overriding federal basis for employing a judicially created, contrary federal rule.

Setting aside specialty areas that have no conceivable bearing here,[19] federal common law may be created where (1) "the rights and obligations of the United States" are implicated, *Texas Indus.*, 451 U.S. at 641; (2) there is "some congressional authorization to formulate substantive rules of decision," *id.*; or (3) "rules . . . may be necessary to fill in interstitially or otherwise effectuate the statutory patterns enacted in the large by Congress," *DelCostello v. International Bhd. of Teamsters*, 462 U.S. 151, 160 (1983). None of these rationales for creating a uniform federal common law rule of decision are present here, nor does the fact that this case involves the assertion of claims against a former director and officer of a federally chartered institution otherwise give rise to "a significant conflict between

[19] Federal common law may be created, *inter alia*, in cases that involve "interstate and international disputes implicating the conflicting rights of States or our relations with foreign nations, and admiralty cases." *Texas Indus., Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630, 641 (1981) (footnote omitted).

some federal policy or interest and the use of state law."[20] *Wallis*, 384 U.S. at 68.

C. The Rights And Obligations Of The United States Are Not At Issue In This Case

The rights and obligations of the United States are in no way implicated by this case. In *O'Melveny*, the FDIC cited *United States v. Kimbell Foods*, 440 U.S. 715, 726 (1979), for the proposition that " 'federal law governs questions involving the rights of the United States arising under nationwide federal programs.' " 114 S. Ct. at 2053. The Court made clear, however, that "the FDIC is not the United States, and even if it were we would be begging the question to assume that it was asserting its *own* rights rather than, as receiver, the rights of [the failed institution]." *Id.* (emphasis in original). Similarly, here, the United States is not a party to the case and neither the RTC, nor the FDIC as its successor, is the United States. The RTC instituted suit against petitioner in its capacity as receiver of City Federal and seeks to recover only on behalf of the failed institution, not on behalf of the United States.

[20] The court below stated, "The defendants concede that before receivership City Federal . . . had a right to bring an action against them under federal common law." 57 F.3d at 1245, Pet. App. A28. Petitioner respectfully submits that the court is in error on this point. Petitioner's brief to the Third Circuit expressly argued that the RTC's position regarding the existence of a federal common law simple negligence standard of liability was incorrect because the *Briggs* and *Bowerman* cases upon which such argument was based "were decided long before *Erie*," and do not " 'create a federal common law claim, as opposed to being grounded in a state law claim.' " Br. of Appellees at 21 (quoting *FDIC v. Gonzalez-Gorrondona*, 833 F. Supp. 1545, 1550 (S.D. Fla. 1993)). However, even if the defendants are deemed to have made such a concession below, this Court "is not limited to the particular legal theories advanced by the parties, but rather retains the independent power to identify and apply the proper construction of governing law." *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 99 (1991).

D. Congress Has Not Authorized The Creation Of A Uniform Federal Common Law Standard Of Liability

Nowhere has Congress, explicitly or even by implication, authorized federal courts to create federal common law causes of action or standards of liability for the directors and officers of federally chartered depository institutions. HOLA is a comprehensive federal statute that governs the activities of federally chartered savings associations that are not in receivership. Nowhere in that statute is there any mention of director or officer liability issues, much less any indication that Congress intended federal courts to create federal rules of decision governing the liability of directors and officers of federally chartered depository institutions. HOLA stands in sharp contrast to federal statutory schemes that specifically provide causes of action and duties of care regarding the conduct of entities and individuals in the context of such schemes.[21] The only federal statute of which we are aware that speaks to the question of the liability of

[21] There are a number of such statutes. For example, the Labor-Management Relations Act, 1947 provides that "suit[s] for violation of contracts between an employer and a labor organization representing employees . . . may be brought in any district court of the United States having jurisdiction of the parties . . . ." 29 U.S.C. § 185(a) (1994). The federal securities laws provide that purchasers of securities from issuers who have made untrue statements of material fact or omitted to state material facts may sue such issuers. Securities Act of 1933, 15 U.S.C. §§ 77k(a), 77*l* (1994); Securities Exchange Act of 1934, 15 U.S.C. § 78j (1994). The Employee Retirement Income Security Act of 1974 (ERISA) provides that an ERISA plan "fiduciary shall discharge his duties with respect to a plan . . . with the care, skill, prudence, and diligence . . . that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims . . . ." 29 U.S.C. § 1104(a)(1)(B) (1994). The federal Employers' Liability Act (FELA) provides, "Every common carrier by railroad while engaging in commerce . . . shall be liable in damages to any person suffering injury while he is employed by such carrier in such commerce . . . for such injury or death resulting in whole or in part from the negligence of any of the officers, agents, or employees of such carrier . . . ." 45 U.S.C. § 51 (1994).

directors and officers of federally chartered savings associations is § 1821(k). Nothing in § 1821(k), however, nor in any other part of FIRREA, authorizes federal courts to create liability rules for such directors and officers.

E. There Is No Basis For The Interstitial Use Of Federal Common Law In This Case

There are no interstices to be filled in any federal statute that would justify the creation of federal common law liability standards for directors and officers of federally chartered depository institutions. As indicated, the applicable statute, HOLA, simply does not address the issue of director or officer liability. Therefore, there are no details to be "fleshed out" in the statutory scheme that would justify the creation of federal common law on this basis. This stands in sharp contrast to other federal statutory schemes where Congress has addressed a particular issue and where the Court has approved judicial rulemaking to fill in interstitially the statutory pattern that Congress enacted. *See, e.g., Varity Corp. v. Howe*, 116 S. Ct. 1065, 1070 (1996) (courts may develop a federal common law of rights and obligations for employee benefit plans regulated under ERISA); *Consolidated Rail Corp. v. Gottshall*, 114 S. Ct. 2396, 2410 (1994) (adopting a "common-law zone of danger test as delimiting the proper scope of an employer's duty under FELA to avoid subjecting its employees to negligently inflicted emotional injury").

F. The Fact That City Federal Was Federally Chartered Does Not Give Rise To A "Significant Conflict Between Some Federal Policy Or Interest And The Use Of State Law"

The only significant remaining question is whether federal common law liability standards must be applied in lieu of state law standards simply by virtue of the fact that City Federal was federally chartered rather than state chartered. Some lower court decisions, particularly those rendered before *O'Melveny*, have held that because federally chartered savings associations are subject to comprehensive federal regulation " 'from [their] cradle to [their] corporate grave,' " *Fidelity Fed. Sav. & Loan*

Ass'n v. de la Cuesta, 458 U.S. 141, 145 (1982) (quoting *People v. Coast Fed. Sav. & Loan Ass'n*, 98 F. Supp. 311, 316 (S.D. Cal. 1951)), federal law alone governs their internal affairs, including the issue of director and officer liability. *See, e.g., RTC v. Hess*, 820 F. Supp. 1359, 1362 (D. Utah 1993) ("[F]ederal law exclusively governs the internal affairs of federal savings and loan associations . . . ."); *City Fed. Sav. & Loan Ass'n v. Crowley*, 393 F. Supp. 644, 655 (E.D. Wis. 1975) ("[A] state court adjudicating [the fiduciary duties of directors of a federal savings and loan] would have to apply federal common law rules rather than the laws of its own state."); *Rettig v. Arlington Heights Fed. Sav. & Loan Ass'n*, 405 F. Supp. 819, 826 (N.D. Ill. 1975) ("[O]nly federal law may be applied to questions involving [fiduciary duties of federal savings and loan directors].").

We respectfully suggest that these and similar cases have been wrongly decided. It is, of course, indisputable that federally chartered savings associations have been subject to extensive federal regulation both under the terms of HOLA and the regulations promulgated pursuant thereto by the FHLBB (prior to FIRREA) and the OTS (since FIRREA). Indeed, this Court has indicated that, while it was in existence, the FHLBB's authority to regulate federally chartered savings associations was virtually unlimited. *Fidelity Fed.*, 458 U.S. at 144. Accordingly, when HOLA or regulations promulgated thereunder by the FHLBB or OTS address a particular question pertaining to federally chartered savings associations, any conflicting state rule is perforce preempted.[22] Yet, despite the breadth of HOLA and the

[22] The preemption doctrine is rooted in the Supremacy Clause, U.S. Const. art. VI, cl. 2. If Congress intends, either explicitly or implicitly, to displace state law completely, the federal statute or regulation will supersede the state rule. *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230, *rev'd on other grounds sub nom., Rice v. Board of Trade*, 331 U.S. 247 (1947). Where Congress has not completely displaced state regulation in a particular area, federal law may still preempt state law where "compliance with both federal and state [law] is a physical impossibility," *Florida Lime & Avocado Growers, Inc., v. Paul*, 373 U.S. 132, 142-43 (1963), or where the

(footnote continues)

regulations thereunder governing federal savings associations, one will search them in vain for a single provision that addresses the standard of director or officer liability for breach of the duty of care. There can be no "significant conflict," *O'Melveny*, 114 S. Ct. at 2055, between the use of state law standards of liability for directors and officers of federally chartered institutions and any identifiable federal policy or interest respecting such standards because HOLA and the regulations thereunder simply do not address the issue.

Indeed, the fact that HOLA and the FHLBB and OTS regulations create a "comprehensive scheme" of federal regulation of federally chartered institutions itself precludes creation of supplementary federal common law causes of action or standards of liability respecting directors and officers of federally chartered savings associations in lieu of state law causes of action and standards of liability that would otherwise apply. This point was made decisively in *O'Melveny*. The Court acknowledged that if there is "an explicit federal statutory provision," then of course state law is displaced. *O'Melveny*, 114 S. Ct. at 2054. But state law does not have to give way to judge-made federal common law merely where, as here, the federal scheme is comprehensive: "Nor would we adopt a court-made rule to supplement federal statutory regulation that is comprehensive and detailed; *matters left unaddressed in such a scheme are presumably left subject to the disposition provided by state law.*" *Id.* (emphasis added).

Indeed, the Court recognized in *O'Melveny* that FIRREA constitutes "comprehensive legislation." *Id.* at 2054. Accordingly, the Court ruled that this gives courts no authority to "supplement" FIRREA with common law exceptions to the statutory scheme. *Id.* In like manner, the fact that HOLA and the regulations promulgated by the FHLBB and OTS constitute a comprehensive federal regulatory scheme for federally chartered savings

(footnote continued)

state rule is "an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941).

associations precludes federal courts from "supplement[ing]" that scheme with federal common law rules respecting the liability of directors and officers of such associations for ordinary negligence. It is noteworthy that the Court has declined to authorize the creation of federal common law in other contexts where the federal regulatory scheme undeniably has been comprehensive. *See, e.g., Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 97-100 (1991) (refusing to adopt a federal common law rule of demand futility in an action founded on the Investment Company Act of 1940); *Burks v. Lasker*, 441 U.S. 471, 480-86 (1979) (refusing to adopt a federal common law rule respecting termination of derivative actions by directors under the Investment Company Act of 1940 and the Investment Advisers Act of 1940); *United States v. Kimbell Foods, Inc.*, 440 U.S 715, 718 (1979) (refusing to adopt a federal common law rule of lien priority for federal loan programs, holding that "a national rule is unnecessary to protect the federal interests underlying the loan programs").

The fact that Congress has clearly shown an interest in the regulation of federally chartered savings associations, as evidenced by the provisions of HOLA that govern the powers and operations of such associations, cannot be read as authorization for federal courts to apply federal common law in this area. The Court soundly rejected the FDIC's argument in *O'Melveny* "that FIRREA as a whole, by demonstrating the high federal interest in this area, confirms the courts' authority to promulgate [federal] common law." 114 S. Ct. at 2054. *See also Boyle v. United Technologies Corp.*, 487 U.S. 500, 507 (1988) (determination that "procurement of equipment by the United States is an area of uniquely federal interest does not . . . end the inquiry" into whether state law applies; "[d]isplacement [of state law and its replacement by federal common law rules] will occur only where, as we have variously described, a 'significant conflict' exists between an identifiable 'federal policy or interest and the [operation] of state law,' or the application of state law would 'frustrate specific objectives' of federal legislation" (quoting *Wallis*, 384 U.S. at 68, and *Kimbell Foods*, 440 U.S. at 728)).

It may be suggested that *O'Melveny* is inapposite because the Court there was asked to create a new federal common law rule of decision regarding imputation of knowledge whereas here the Court is merely being asked to permit the application of "well established" federal common law to claims against directors and officers of federally chartered institutions. *Cf. Motorcity of Jacksonville, Ltd. v. Southeast Bank N.A.*, 83 F.3d 1317 (11th Cir. 1996) (holding that *O'Melveny* did not apply to the "previously-established and longstanding federal common-law *D'Oench* doctrine").[23] *But cf. DiVall Insured Income Fund Ltd. Partnership v. Boatmen's First Nat'l Bank*, 69 F.3d 1398, 1402 (8th Cir. 1995) (relying on *O'Melveny* to hold that the *D'Oench* doctrine was preempted by FIRREA); *Murphy v. FDIC*, 61 F.3d 34, 38 (D.C. Cir. 1995) (same).[24] The plain fact is, however, that, despite the venerable age of *Briggs*, the federal common law respecting the liability standards for directors and officers of federally chartered depository institutions is anything but "well established." As noted above, it is at least arguable that *Briggs* and *Bowerman* both articulate a gross negligence standard of liability. *See supra* pp. 32-34. Cases since *Briggs* have reached no consensus on what the federal common law standard, if any, should be.[25] The FDIC is hardly in a position to deny this. It has candidly, and accurately, admitted that "[t]he content of the federal common law standard . . . is not clearly established." Br. for the Resp. in Opp. at 16-17. Indeed, so little "well established"

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[23] The "federal common-law *D'Oench* doctrine" was announced by the Court in *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942). The doctrine "prevents plaintiffs from asserting as either a claim or defense against the FDIC oral agreements or 'arrangements.'" *Adams v. Zimmerman*, 73 F.3d 1164, 1168 (1st Cir. 1996) (quoting *Timberland Design, Inc. v. First Serv. Bank for Sav.*, 932 F.2d 46, 48-50 (1st Cir. 1991)).

[24] Other circuit courts have suggested, in dicta, that the federal common law *D'Oench* doctrine did not survive FIRREA and *O'Melveny*. *Dimuzio v. RTC*, 68 F.3d 777, 780 (3d Cir. 1995); *RTC v. Kennelly*, 57 F.3d 819, 822 n.3 (9th Cir. 1995).

[25] *See RTC v. Chapman*, 29 F.3d 1120, 1127 (7th Cir. 1994) (Posner, J., dissenting) ("[I]t is also unclear . . . just what the federal common law rule is. . . . [T]he cases are all over the lot.").

is the federal common law standard, even in 1996, that the court below found it necessary to remand the case to the district court to determine initially what standard of liability applies under federal common law. 57 F.3d at 1247 n.16, 1249, Pet. App. A32, A37.

For this same reason, it is implausible to argue that federal common law should be applied to the directors and officers of federally chartered institutions to assure that the liability standards for all such directors and officers will be uniform. The federal courts have had over a century since *Briggs* to develop a uniform common law standard and they have not done so yet. Unless this Court itself establishes a standard unequivocally, there is no reason to believe that federal common law standards will be any more uniform than state law standards. With thirteen federal circuit courts and hundreds of federal district courts, there can certainly be as much diversity at the federal court level as there is among the states.

Moreover, Congress and the regulators have given no indication that they regard achieving uniformity to be an important federal policy. HOLA has been in existence for more than 50 years and has been amended many times. Yet Congress has never seen fit to articulate a uniform standard of liability for directors and officers of federally chartered savings associations. The failure of Congress and the FHLBB or OTS to create any statutory provisions or rules respecting director or officer liability — in the face of the lack of any uniformity in federal court decisions and given innumerable opportunities to establish uniformity — strongly suggests that uniformity in the standards governing director or officer liability has not been considered to be a significant federal policy interest.

Indeed, in § 1821(k) itself Congress has provided that the term "gross negligence" shall be "defined and determined under applicable State law." That indicates that Congress had no aversion to the use of state law in resolving director and officer liability questions for federally chartered institutions and, indeed, had an obvious preference for the application of state

law to federal common law in this instance. After all, Congress could have set forth its own definition of "gross negligence" or could have specified that the federal courts shall define the term. Of course, by specifying that state law should be consulted for the definition of gross negligence for § 1821(k) purposes, Congress necessarily recognized that there may be a lack of uniformity in definitions. That obviously not only did not bother Congress; it is the result that Congress consciously chose. *See Reconstruction Fin. Corp. v. Beaver County*, 328 U.S. 204, 209 (1946) (where part of regulatory scheme relies on state law, "assumption" that uniformity is necessary cannot be made).[26]

In the past few years, several courts have ruled that state law is inapplicable to the directors and officers of federally chartered institutions by virtue of the so-called "internal affairs" doctrine. *See, e.g., RTC v. Chapman*, 29 F.3d 1120, 1122-24 (7th Cir. 1994); *RTC v. Gladstone*, 895 F. Supp. 356, 363 (D. Mass. 1995); *RTC v. Camhi*, 861 F. Supp. 1121, 1126 (D. Conn. 1994). That doctrine holds that "the law of the state of incorporation normally determines issues relating to the internal affairs of a corporation." *First Nat'l City Bank v. Banco Para el Comercio Exterior*, 462 U.S. 611, 621 (1983). Courts that rely on the doctrine to deny the applicability of state law to director or officer liability contend that, just as the law of the state of incorporation

[26] It is noteworthy in this respect that this Court has refused to fashion a federal rule of decision regarding an issue that falls within an area traditionally governed by state law. *See United States v. Yazell*, 382 U.S. 341, 352 (1966) ("Both theory and the precedents of this Court teach us solicitude for state interests . . . ."); *United States v. Brosnan*, 363 U.S. 237, 242 (1960); *Beaver County*, 328 U.S. at 210 (courts should apply state law to issues that are "deeply rooted in state traditions, customs, habits, and laws").

The standard of director and officer liability at issue in this case falls squarely within two traditional areas of state law: tort law and corporation law. Tort law is among the most fundamental areas of state law. *See Erie R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938). Similarly, issues of corporate law are traditionally a matter of state law. *See Business Roundtable v. SEC*, 905 F.2d 406, 412 (D.C. Cir. 1990) (vacating an SEC rule that would "overturn or at least impinge severely on the tradition of state regulation of corporate law").

resolves issues relating to the internal affairs of a state chartered corporation, so federal law should control the internal affairs of a federally chartered depository institution. *Chapman* is the leading case espousing application of the internal affairs doctrine to federally chartered savings associations. 29 F.3d 1120. The Seventh Circuit there held that the RTC had no assertable state law claim against the directors and officers of a federally chartered savings association because, while "there is no federal corporate code," the "[f]ederal courts have no less authority to shape a common law for federal corporations than state courts have had to devise a common law for firms incorporated in their jurisdictions." *Id.* at 1123.

We submit that application of the internal affairs doctrine in the present context is inappropriate. The doctrine is a conflict of laws principle that properly applies where a choice must be made between the laws of two or more states. *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982). The doctrine has no application here, where the "choice" is between the application of state law or federal common law rules of decision. *O'Melveny* provides the guidelines for determining how that choice is to be made. Remarkably, even though *Chapman* was decided shortly after *O'Melveny*, the Seventh Circuit never mentions *O'Melveny* in its opinion. A number of recent cases have recognized, however, that application of the internal affairs doctrine to the liability of directors and officers of federally chartered associations is inconsistent with *O'Melveny*. Accordingly, they have ruled that state law, not federal common law, governs such liability. *See, e.g.*, *FDIC v. Cohen*, 95 Civ. 683 (LLS), 1996 U.S. Dist. LEXIS 2247, at *27 (S.D.N.Y. Feb. 28, 1996) (federal law does not govern the liability of the directors of a federally chartered bank "because the creation of a federal common law is disfavored"); *FDIC v. Abel*, 92 Civ. 9175 (JFK), 1995 U.S. Dist. LEXIS 18159, at *15 (S.D.N.Y. Dec. 5, 1995) ("[S]tate law claims may be brought against directors and officers of federally-chartered banks. . . ."); *FDIC v. Raffa*, 882 F. Supp. 1236, 1244 (D. Conn. 1995) ("[T]he mere fact that a financial institution is federally chartered does not immunize that institution from state law."); *RTC v. Gregor*, 872 F. Supp. 1140, 1146 (E.D. N.Y. 1994) (in light of *O'Melveny*, pre-FIRREA state law provides the applicable standard of care for directors and officers of federally chartered institutions); *RTC v. Fiala*, 870 F. Supp. 962, 969 (E.D. Mo. 1994) ("The Court finds the state/federal distinction . . . nonsensical."). *See also RTC v. Gibson*, 829 F. Supp. 1103, 1109 n.2 (W.D. Mo. 1993) ("There is nothing to suggest that officers and directors of federally chartered institutions are only subject to federal causes of action.").

Indeed, the Court has already made clear that state law can apply to the internal affairs of a federally chartered savings association. In *California Fed. Sav. & Loan Ass'n v. Guerra*, 479 U.S. 272 (1987), the Court affirmed the application of a state employment discrimination law to a federally chartered savings association that had failed to reinstate an employee returning from pregnancy disability leave to the job she had previously held. *Cf. Wichita Royalty Co. v. City Nat'l Bank*, 306 U.S. 103 (1939) (applying state law to tort claim by depositor against directors of national bank). Other courts have reached similar results. *See, e.g.*, *Goldman v. First Nat'l Bank*, 985 F.2d 1113, 1121 (1st Cir. 1993) (state law claim by former employee of national bank for breach of employment contract); *Austin v. Altman*, 332 F.2d 273, 276 (2nd Cir. 1964) (in action by shareholders of national bank against bank directors for various alleged improprieties in connection with the organization of the bank, the court held the case was not "a federal matter merely because the bank is chartered under federal law").[27]

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[27] Other courts have applied state laws to employment disputes and other internal affairs of other federally chartered entities such as Amtrak and the American Red Cross. *See, e.g.*, *Hirras v. National R.R. Passenger Corp.*, 44 F.3d 278 (5th Cir. 1995) (holding that an Amtrak employee may proceed with state law negligent infliction of emotional distress claim against Amtrak where the elements of the claim are factual questions that pertain to the conduct of the employee and the employer); *Cummings v. National R.R. Passenger Corp.*, 514 Pa. 230, 523 A.2d 338 (state law breach of employment contract claim by an Amtrak employee against Amtrak),

(footnote continues)

In accordance with the authorities discussed above, we submit that state law claims for negligence apply to the directors and officers of federally chartered savings associations of their own force. But, even if it were the case that federal law governs the issue of the standard of liability of directors and officers of federally chartered institutions in the first instance, that "does not much advance the ball." *O'Melveny*, 114 S. Ct. at 2053. As the Court in *O'Melveny* noted, application of federal law "includes federal adoption of state-law rules." *Id. See also Boyle*, 487 U.S. at 508 n.3; *Kimbell Foods*, 440 U.S. at 726; *United States v. Little Lake Misere Land Co.*, 412 U.S. 580, 594 (1973). It is only when a "significant conflict" exists between the application of such state law rules of decision and an identifiable federal policy that any basis exists for the creation of a uniform federal common law rule of decision. *O'Melveny*, 114 S. Ct. at 2055; *Boyle*, 487 U.S. at 508; *Wallis*, 384 U.S. at 68. As demonstrated above, no such "significant conflict" exists in this case.

Accordingly, there never was before the enactment of § 1821(k), and there is not now, any justification for the creation or application of a uniform federal common law rule of decision regarding the standard of liability for directors and officers of federally chartered savings associations. Any claims that the RTC or FDIC may have against the directors and officers of federally chartered savings associations are assertable only under § 1821(k) for gross negligence or under state law for simple negligence in the applicable states recognizing a simple negligence standard of liability.

(footnote continued)

cert. denied, 484 U.S. 852 (1987); *American Nat'l Red Cross v. Labor Relations Comm'n*, 363 Mass. 525, 296 N.E.2d 214 (1973) (applying Massachusetts law to regulate the labor practices of the local Red Cross chapter).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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